Supreme Court, U. S.
FILED
JUN 13 1979
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-986

ARKANSAS LOUISIANA GAS COMPANY, *Petitioner,*

v.

FRANK J. HALL, MRS. W. E. HALL, SR., THE H. M. HARRELL TESTAMENTARY TRUST, JAMES E. HARRELL, JOHN K. HARRELL, SR., ASA BENTON ALLEN, SIDNEY G. MYERS, JR., W. O. COCHRAN, THOMAS F. PHILYAW, MRS. ELAINE ALLEN, JAMES A. NOE, D. B. MCCONNELL, MRS. EVA L. WEISS, SOL KAPLAN and NATIONAL AMERICAN BANK, New Orleans, Co-Testamentary Executors of the SUCCESSION of SEYMOUR WEISS, *Respondents.*

PETITIONER'S REPLY TO BRIEF FOR THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION AS AMICI CURIAE

ROBERT ROBERTS, JR.
MARLIN RISINGER, JR.
W. MICHAEL ADAMS
BLANCHARD, WALKER, O'QUIN & ROBERTS
Post Office Drawer 1126,
Shreveport, Louisiana 71163

Counsel for Petitioner

REUBEN GOLDBERG
GLENN W. LETHAM
GOLDBERG, FIELDMAN & LETHAM, P.C.
1700 Pennsylvania Ave., N.W.
Washington, D.C. 20006

Of Counsel

PRESS OF BYRON S. ADAMS PRINTING, INC., WASHINGTON, D. C.

INDEX

Page

TABLE OF AUTHORITIES ii

I. This Case Requires the Exercise of the Commission's Special Expertise 4

A. Expertise as to Triggering of the Favored Nation Clause 4

B. Commission Expertise for Comparison of the Rate Schedule with the Government Lease and Determining the Proper Application of the Area Rate to a Price Adjustment 9

II. Federal Law Requires Uniformity of Rate Regulation under the Natural Gas Act 13

A. The Paramount Nature of Federal Regulatory Law 15

B. *Mobil Oil Corp.* v. *FPC* is Relevant to the Meaning of the Favored Nation Clause 19

C. The Solicitor's Reliance on *Skelly* and *Pan American* is Misplaced 23

(i) *Skelly Oil Co.* v. *Phillips Petroleum Co.* .. 23

(ii) *Pan American Petroleum Corp.* v. *Superior Court* 25

III. The State Court Decisions Infringe on the Commission's Regulatory Responsibilities under the Natural Gas Act 28

IV. Conclusion 32

CASES: Page

Appalachian Power Co. v. FPC, 529 F.2d 342 (D.C. Cir. 1976), cert. denied, 429 U.S. 816 (1976) ... 7, 16, 25
Ashland Oil and Refining Co. v. FPC, 421 F.2d 17 (6th Cir. 1970) ... 18
Atlantic Refining Co. v. Public Service Commission, 360 U.S. 378 (1959) ... 14
Bel Oil Corp. v. FPC, 255 F.2d 548 (5th Cir. 1958) ... 18
Brooklyn Union Gas Co. v. Transcontinental Gas Pipe Line Corp., 201 F. Supp. 673 (S.D. Tex. 1960) ... 18
Burnet v. Harmel, 287 U.S. 103 (1932) ... 20
California v. Southland Royalty Co., 436 U.S. 519 (1978) ... 17
Colorado Interstate Gas Co. v. FPC, 324 U.S. 581 (1945) ... 18
Columbia Gas Transmission Corp. v. FPC, 530 F.2d 1056 (D.C. Cir. 1976) ... 7
El Paso Natural Gas Co., 29 F.P.C. 1175 (1963) ... 12, 29-30
FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972) ... 4
FPC v. Sierra Pacific Power Co., 350 U.S. 348 (1956) .. 6, 16
FPC v. Southern California Edison Co., 376 U.S. 205 (1964) ... 16
FPC v. Tennessee Gas Transmission Co., 371 U.S. 145 (1962) ... 4
FPC v. Texaco Inc., 417 U.S. 380 (1974) ... 17
FPC v. Transcontinental Gas Pipe Line Corp., 365 U.S. 1 (1961) ... 4
Gulf States Utilities Co. v. FPC, 518 F.2d 450 (D.C. Cir. 1975) ... 7
Gully v. First National Bank, 299 U.S. 109 (1936) 26
Indiana & Michigan Electric Co. v. FPC, 530 F.2d 1060 (D.C. Cir. 1976) ... 7
Jicarilla Apache Tribe v. FERC, 578 F.2d 289 (10th Cir. 1978) ... 17, 18, 21, 22
Lewis v. Transcontinental Gas Pipe Line Corp., 200 F. Supp. 219 (S.D. Tex. 1961) ... 27
Lone Star Gas Co. v. Howard Corp., 556 S.W.2d 372 (Tex. Ct. of Civ. App. 1977) ... 16
McLeran v. El Paso Natural Gas Co., 357 F. Supp. 329 (S.D. Tex. 1972), affirmed 491 F.2d 405 (5th Cir. 1974) ... 19

Page

Mississippi Power & Light Co. v. Memphis Natural Gas Co., 162 F.2d 388 (5th Cir. 1947) cert. denied 332 U.S. 769 (1947) ... 18
Mississippi Power & Light Co. v. United Gas Pipe Line Co., 532 F.2d 412 (5th Cir. 1976) ... 8
Mobil Oil Corp. v. FPC, 483 F.2d 1238 (D.C. Cir. 1973) ... 12, 29
Mobil Oil Corp. v. FPC, 463 F.2d 256 (D.C. Cir. 1971) cert. denied sub nom., Mobil Oil Corp. v. Matzen, 406 U.S. 976 (1972) ... 17, 19-23, 25
Morris Mizel, et al., 30 F.P.C. 1103 (1963) ... 6, 25
NAACP v. FPC, 425 U.S. 662 (1976) ... 4
Natural Gas Pipe Line Co. v. Harrington, 246 F.2d 915 (5th Cir. 1957) ... 18
New England Power Co. v. FERC, 571 F.2d 1213 (D.C. Cir. 1977) ... 7
Northern Natural Gas Co. v. State Corp. Commission, 372 U.S. 84 (1963) ... 15
Pan American Petroleum Corp. v. Superior Court, 366 U.S. 656 (1961) ... 23, 25-28
Permian Area Rate Case, 390 U.S. 747 (1968) ... 12, 29
Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954) ... 4, 14, 16, 24, 31
Shell Oil Co., 29 F.P.C. 498 (1963) ... 4-5, 8
Skelly Oil Co. v. Phillips Petroleum Co., 339 U.S. 667 (1950) ... 23-25, 26
Socony Mobil Oil Co. v. Brooklyn Union Gas Co., 299 F.2d 692 (5th Cir. 1962), cert. denied 371 U.S. 887 (1962) ... 18, 27
Stratton's Independence v. Howbert, 231 U.S. 399 (1913) ... 21
Sunray Mid-Continent Oil Co. v. FPC, 364 U.S. 137 (1960) ... 4, 17
Sunray Mid-Continent Oil Co. v. FPC, 290 F.2d 552, 555 (10th Cir. 1961) ... 29, 30
Superior Oil Co. v. El Paso Natural Gas Co., 377 S.W. 2d 691 (Tex. Ct. of Civ. App. 1964) ... 15, 16
Tenneco Oil Co. v. FERC, 580 F.2d 722 (5th Cir. 1978) ... 18, 31
United Gas Improvement Co. v. Continental Oil Co., 381 U.S. 392 (1965) ... 4, 14, 15, 17
United Gas Pipe Line v. Memphis Light, Gas & Water Division, 358 U.S. 103 (1958) ... 6, 7

Page

United Gas Pipe Line Co. v. Mobile Gas Service Corp., 350 U.S. 332 (1956) 6, 16
Von Baumbach v. Sargent Land Co., 242 U.S. 503 (1916) 21
West Texas Gathering Co., 29 F.P.C. 510 (1962) 6

STATUTES:

Federal Power Act, 16 U.S.C. §§ 791, *et seq.* 6
Natural Gas Act, 15 U.S.C. §§ 717, et seq. ..... *passim*
Natural Gas Act, 15 U.S.C. § 717f(c) 24
Natural Gas Policy Act of 1978, 92 Stat. 3350 (1978) .. 13

MISCELLANEOUS:

Order on Rehearing of Order No. 23, "Amendment and Clarification of the Commission's Interim Regulations Implementing the Natural Gas Policy Act of 1978 and Regulations Under the Natural Gas," 44 F.R. 30681 (May 29, 1979) 13

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-986

ARKANSAS LOUISIANA GAS COMPANY, *Petitioner*,

v.

FRANK J. HALL, MRS. W. E. HALL, SR., THE H. M. HARRELL TESTAMENTARY TRUST, JAMES E. HARRELL, JOHN K. HARRELL, SR., ASA BENTON ALLEN, SIDNEY G. MYERS, JR., W. O. COCHRAN, THOMAS F. PHILYAW, MRS. ELAINE ALLEN, JAMES A. NOE, D. B. MCCONNELL, MRS. EVA L. WEISS, SOL KAPLAN and NATIONAL AMERICAN BANK, New Orleans, Co-Testamentary Executors of the SUCCESSION of SEYMOUR WEISS, *Respondents*.

PETITIONER'S REPLY TO BRIEF FOR THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION AS AMICI CURIAE

Petitioner, ARKANSAS LOUISIANA GAS COMPANY ("Arkla"), hereby replies to the Brief for the United States and the Federal Energy Regulatory Commission as Amici Curiae filed by the Solicitor General of the United States on June 2, 1979.

The Solicitor General and the Federal Energy Regulatory Commission ("Commission") phrase the question presented as:

> "Whether, in an action for breach of a gas purchase contract subject to the Natural Gas Act, the

state courts should have referred the interpretation of the disputed contract provision to the Federal Energy Regulatory Commission under the primary jurisdiction doctrine."

But all contractual disputes are not as germane to Commission jurisdiction as are those concerning price. Since all issues of this case pertain to *increased* prices payable under the gas purchase contract, the question presented is more precisely stated by the addition of the two words "price increase" as follows:

> "Whether, in an action for breach of a gas purchase contract subject to the Natural Gas Act, the state courts should have referred the interpretation of the disputed *price increase* contract provision to the Federal Energy Regulatory Commission under the primary jurisdiction doctrine."

The Solicitor General and the Commission recognize that the Commission has primary jurisdiction to consider the reasonableness of rates and practices to prevent disruption of the regulatory scheme and the unbalancing of existing rate structures. However, they argue that no such issues are presented in this case (Brief for the United States, p. 15). Further, they submit that, in the instant case, the Louisiana Court of Appeal correctly declined to refer the interpretation of the favored nation clause to the Commission under the primary jurisdiction doctrine and, thus, there is no reason for further review by this Court (Brief of the United States, p. 10).

In regard to primary jurisdiction, the Solicitor General and the Commission state that whether the Commission's primary jurisdiction should be invoked in any particular contract dispute involving the interstate sale of natural gas depends upon:

> "the public interest considerations that inform the primary jurisdiction doctrine, as applied to the particular case. These include the need for the exercise by the Commission of its special expertise in the circumstances of the case; the need for uniformity of interpretation; and the impact of the issues on the regulatory responsibilities of the agency." Brief for the United States, p. 13.

An analysis of these public interest considerations in light of the arguments of the Solicitor General and the Commission and the decisions of the Louisiana courts for which review is sought show that the Solicitor General and the Commission have misconstrued the doctrine of primary jurisdiction as it applies to the Commission's rate jurisdiction under the *Natural Gas Act,* 15 U.S.C. §§ 717, *et seq.* Furthermore, the question here is whether the state courts should have referred the questions presented in this case to the Commission. The Commission and the courts, in dealing with questions of the same nature as those involved in this case, have recognized the need for exercise of the Commission's special expertise; and have recognized the need for uniformity and the paramount nature of federal regulatory law.

Petitioner submits that the position of the Solicitor General and the Commission that this case does not present issues coming within the above quoted criteria they recognize for requiring reference to the Commission is contrary to prior policies and decisions by the Commission in administering and enforcing the *Natural Gas Act,* as well as decisions by the courts. Petitioner further submits that the position of the Solicitor General and the Commission is a withdrawal by the Commission from its regulatory responsibilities under the *Natural Gas Act* which it has heretofore recognized

and performed and from the standards for the interpretation of the *Natural Gas Act,* and of gas sales contracts and other questions arising under the *Natural Gas Act.* This Court has declared as follows:

> "Protection of consumers against exploitation at the hands of the natural gas companies was the primary purpose of the Natural Gas Act."

Phillips Petroleum Co. v. *Wisconsin,* 347 U.S. 672, 685 (1954); *United Gas Improvement Co.* v. *Continental Oil Co.,* 381 U.S. 392 (1965); *FPC* v. *Transcontinental Gas Pipe Line Corp.,* 365 U.S. 1 (1961); *Sunray Mid-Continent Oil Co.* v. *FPC,* 364 U.S. 137 (1960); *NAACP* v. *FPC,* 425 U.S. 662 (1976); *FPC* v. *Tennessee Gas Transmission Co.,* 371 U.S. 145 (1962); *FPC* v. *Louisiana Power & Light Co.,* 406 U.S. 621 (1972).

I.

THIS CASE REQUIRES THE EXERCISE OF THE COMMISSION'S SPECIAL EXPERTISE

A. Expertise as to Triggering of the Favored Nation Clause.

The principal issue in the lawsuit is whether the payment of market value royalties by Petitioner to the United States under a Government lease is a "purchase from another party seller" which would "trigger" the Section 8(D) favored nation clause of Respondents' Gas Rate Schedule. The Commission has considered this precise issue on many occasions and has developed its own special rules and regulations regarding the "triggering" of favored nation clauses. The Commission is uniquely aware of the principles that are involved in making that determination. In *Shell Oil Co.,* 29 F.P.C. 498, 499-500 (1963), the Commission stated what it considered to be the burden of proof on

a producer in order for the Commission to hold that a favored nation clause had been triggered by the purchaser paying another producer a higher rate:

> "[I]n order for the 'triggering' to occur, where (as here) the contract so provides, the producer filing the most-favored-nation rate increase must show that the other producer is the type of seller contemplated and produces in the area indicated in the contract, that the gas being purchased from the other producer is comparable gas, and that the rate being paid for it is 'higher' in fact as well as in appearance. By showing that these and any other conditions precedent (to triggering) exist, the producer filing for the escalated increase shows that his proposed increase has the 'contractual support' or consent of his purchaser; and the increased rate may be accepted for filing. *If he fails to show that these necessary conditions exist, his filing is rejected as a contractually unauthorized, unilateral rate increase.*" [Emphasis added.]

Respondents must have established to the Commission that they have contractual support for the activation of the favored nation clause before an increase in rate can become effective.

Additionally, however, the Commission further requires that producers must show that,

> "[a]fter establishing what rate is valid under the contract clause for the favored-nation increase, it must be shown that such rate is just and reasonable. In sum, *the validity of his filing is at all times subject to the ultimate determination of the validity of the triggering rate as well as the justness and reasonableness of the increased rate.*" 29 F.P.C. at 504. [Emphasis added.]

Thus, the Commission has established its own guidelines as to when a favored nation clause is triggered.

The issue of whether the payment of market value royalties under a Government lease is a "purchase" of gas that would constitute a basis for a change of rates for the sale of interstate natural gas should have been determined by the Commission in the first instance without resort to the state courts of Louisiana. See also, *West Texas Gathering Co.*, 29 F.P.C. 510 (1962), and *Morris Mizel, et al.*, 30 F.P.C. 1103 (1963). In the latter case, the Commission held based on a plain meaning rule of contract construction that a farmout agreement did not constitute a "purchase" sufficient to activate a favored nation clause:

> "In the absence of any provision in the Mizel-Trusts contract to the contrary, we must assume that the word 'purchase' is used as it is commonly employed in the industry, *i.e.*, in reference to the standard gas purchase contract." 30 F.P.C. at 1104.

Clearly, Commission expertise is required to insure proper application of established Commission rules and the decisions of appellate courts in review of Commission orders and opinions under the *Natural Gas Act*.

In this context, the Commission has regularly interpreted contracts on file with it as rate schedules. Indeed, under the *Mobile-Sierra-Memphis*[1] trilogy of cases, the Commission would always decide in the first instance whether a particular rate increase filing would be contractually authorized. In reviewing the Commission's decisions as to the "contract interpretation," the appellate courts have uniformly deferred to the Commission's expertise if its decision is amply supported both factually and legally. In *Gulf States Utilities Co.* v. *FPC*, 518 F.2d 450, 457 (D.C. Cir. 1975), it was stated:

> "Although the application of *Mobile-Sierra Memphis* principles to a given contract is primarily a matter of law, where the decision involves the interpretation of the parties' intent as revealed in the language of a contract, it is proper to defer to the Commission's expertise if its decision is 'amply supported both factually and legally.' *United Gas Pipe Line Co.* v. *Memphis Light, Gas & Water Division*, 358 U.S. [103 ,114 (1958).]"

Other cases embodying this same rule of law are numerous. See, *e.g.*, *Appalachian Power Co.* v. *FPC*, 529 F.2d 342, 351 (D.C. Cir. 1976), *cert. denied*, 429 U.S. 816 (1976)[2]; *Columbia Gas Transmission Corp.* v. *FPC*, 530 F.2d 1056, 1059 (D.C. Cir. 1976); *Indiana & Michigan Electric Co.* v. *FPC*, 530 F.2d 1060, 1062 (D.C. Cir. 1976); *New England Power Co.* v. *FERC*, 571 F.2d 1213 (D.C. Cir. 1977).

It has also been held that the Commission's primary jurisdiction under the *Natural Gas Act* is so extensive that it should be recognized even in the context of a non-jurisdictional rate setting where a Com-

---

[1] *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.* ("*Mobile*"), 350 U.S. 332 (1956); *FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956) ("*Sierra*"); *United Gas Pipeline Co.* v. *Memphis Light, Gas & Water Division*, 358 U.S. 103 (1958). The trilogy has been held to apply equally to the *Natural Gas Act* and the *Federal Power Act*, 16 U.S.C. §§ 791, *et seq.*

[2] In *Appalachian Power Co.*, the Commission again relied upon the plain language of the agreements. The Commission declined to take the parties' conduct into account because "only contracts, as filed with the Commission, along with any properly filed and accepted amendments, can be regarded as embodying the presently effective contractual rates, terms and conditions." 529 F.2d at 350, n. 59.

mission filed tariff provision would require interpretation. In *Mississippi Power & Light Co.* v. *United Gas Pipe Line Co.*, 532 F.2d 412, 417 (5th Cir. 1976), it was stated with regard to the Commission's primary jurisdiction:

> "The doctrine of primary jurisdiction has evolved as a means of reconciling the functions of administrative agencies with the judicial functions of the courts. When legal disputes develop that directly affect an industry subject to regulation, the need arises to integrate the regulatory agency into the judicial decision making process. One method to accomplish integration is to have the agency pass in the first instance on those issues that are within its competence. In short, the agency should have the first word." [Footnote and citation omitted.]

The rate increase sought by Respondents for the sale of gas to Petitioner in interstate commerce should have been passed upon by the Commission "in the first instance." As concerns jurisdictional rate increases, the Commission "should [certainly] have the first word."

The fact that the Rate Schedule at issue was entered into prior to the adoption of Commission policies prohibiting contracts containing favored nation clauses does not affect the application of the *Shell Oil Co., supra,* criteria. *Shell* dealt with requirements for triggering of a favored nation clause in a contract entered into prior to the adoption of the Commission's policies regarding such clauses. 29 F.P.C. at 499. The same tests would be required here.

B. Commission Expertise for Comparison of the Rate Schedule with the Government Lease and Determining the Proper Application of the Area Rate to a Price Adjustment.

The analysis and comparison of the two contracts at issue require the application of principles that are within the special knowledge and expertise of the Commission. The favored nation provision provides for a comparison of the price provisions of the Rate Schedule with the [3]

> "concurrently effective higher price provisions of such subsequent contract; provided that in determining whether a given price is in fact 'higher' than the price provisions of this contract, the inquiry shall not be limited to the actual prices stipulated but due consideration shall also be given to a comparison of all other pertinent provisions of the two contracts, such as point of delivery, basis of measurement, taxes, dehydration, and delivery pressures . . . ."

In the determination of whether the price is, in fact, higher, and, if so, how much higher, the Commission would have to look to all the other provisions of the contract such as point of delivery, payment for extracted products, base of measurement, taxes, dehydration, delivery pressures, as well as other comparable provisions of the two contracts. Additionally, Respondents have styled their claim in state court as a separate claim for "residue gas" and "extracted plant products." The Rate Schedule provides for the sale of a

---

[3] The Solicitor General and the Commission (Brief for the United States, p. 3) quote only part of the favored nation provision that is Section 8(D) of the Rate Schedule. They leave out the language quoted here that requires "due consideration . . . be given . . . all . . . pertinent provisions of the two contracts. . . ." The entire Section 8(D) is set out at pages 5-6 of the initial petition to this Court.

wellhead stream of gas with all the liquefiable hydrocarbons contained therein:

> "(b) *The prices hereinabove in this Section 8 provided to be paid by Buyer to Seller shall constitute full payment for all gas delivered hereunder and also for all liquefiable hydrocarbons and other products delivered with such gas, it being understood and agreed that any and all products whatsoever recovered or recoverable from the production delivered hereunder by means of any type of processing operation subsequent to delivery shall be the property of Buyer or its assign without any obligation to make further payment to Seller for such products,* it being further understood and agreed, however, that nothing herein is intended to deprive Seller of the right to operate a standard type oil field separator at each well subject hereto in order to remove such condensate as may be thereby extracted prior to delivery of production hereunder to Buyer. The parties take cognizance of the fact that the aforesaid prices hereinabove provided to be paid are $0.0025 per MCF higher than would have been provided had Seller retained the right to participate in the recovery of products by such processing operations subsequent to delivery, and accordingly the aforesaid prices have been calculated and agreed to by the parties with the intention and understanding that payment of the said prices shall constitute payment for all products whatsoever recoverable from the production delivered to Buyer hereunder." [Emphasis added.]

The provision respecting liquid hydrocarbons recovered at the well separator (condensate) is contained in Section 9 as follows:

> "9. *CONDENSATE.* Buyer, or its assign, shall have the option from time to time and upon sixty (60) days' notice, of purchasing all of the free condensate that may be produced from the subject wells and which may be recovered or recoverable by the use of separators operated in connection with such wells, and measured by liquid meter, or liquid gas ratio tests as hereinafter set forth, and shall accept delivery of such condensate into the gas gathering lines or at Seller's option from Seller's storage tanks located on the leases. Buyer, or its said assign, shall deliver to Seller written notice of the exercise of its said option and may discontinue the purchase of condensate by giving Seller sixty (60) days' written notice that it no longer desires to purchase same.
>
> . . . .
>
> Buyer shall pay or cause to be paid to Seller, for condensate received in accordance with the provisions of this Section, the price posted by Buyer or its said assign, as the case may be. Provided, however, that such posted price shall be in line with the prices established by the majority of major oil companies for similar grade condensate in fields in North Louisiana."

Respondents' claims and related calculations require a radical change in the Rate Schedule to provide them with what the contract denies, that is, a separate settlement for the value of the products manufactured from the liquefiable hydrocarbons contained in the gas sold and for the value of the upgraded condensate produced from their gas wells and processed in Petitioner's plant. These complicated issues of comparison require Commission experience and expertise.

The necessity of exercise of the Commission's special expertise is exemplified by the state courts' decisions as to this aspect of the case. The state courts have found that the lease royalty paid by Petitioner to the United States was computed on a price basis below the maximum area rates. This is true of the royalty paid to the

United States on residue gas. But the state courts have awarded to Respondents a recovery computed on the royalty paid to the United States on the residue gas *plus the royalty paid to the United States on liquids extracted and processed from the gas as produced at the well.* The royalty paid to the United States on extracted and processed liquids amounts to more than the royalty paid on the gas.[4]

Under Respondents' Rate Schedule, the gas sold is the gas as produced at Respondents' wells, including all of the extractible liquids contained in the gas as produced, excepting only condensate extractible at the wellhead. The contract price is a price per Mcf of gas with the extractible liquids, except condensate, contained therein. Supra, pp. 10-11. The area rate price under the Commission's regulations applies to sales of natural gas in interstate commerce, and the same area rate applies to residue gas and to gas sold with extractible liquids contained therein. *Permian Basin Area Rate Case,* 390 U.S. 747, 820 (1968); *Mobil Oil Co.* v. *FPC,* 483 F.2d 1238, 1249 (D.C. Cir. 1973); *El Paso Natural Gas Co.,* 29 F.P.C. 1175, 1179-80 (1963). The Louisiana courts, however, have awarded amounts to the Respondents computed on the area rate ceiling for the gas *plus an amount for extractible liquids contained in the gas which is greater* than the amount awarded for the gas. In fact, the total amount awarded is more than double the area rate ceiling applicable to the gas sold with the liquids contained therein, as provided in Respondents' Rate Schedule.

[4] This is because the royalty was paid to the United States on residue gas and on extracted and processed liquids in accordance with the provisions of the lease.

The state courts' award of more than double the applicable area rate ceiling price has resulted even though they state, and evidently intend, that Respondents recover only up to the area rate applicable to the gas as sold under the contract. The difference in the intention and in the action by the state courts results from their lack of expertise in dealing with residue gas, well gas, condensate and extractible liquids in gas, and the application of the area rate ceiling thereto. These matters clearly come within the special expertise of the Commission.[5]

II.

FEDERAL LAW REQUIRES UNIFORMITY OF RATE REGULATION UNDER THE NATURAL GAS ACT

Even though the Solicitor General and the Commission state that the Commission "undoubtedly" has primary jurisdiction over rate regulation, it is argued that the Commission's role should intrude no further into state law than necessary to carry out the Commission's responsibilities under the *Natural Gas Act.* It is only because the Commission's role would involve interpretation of a contract that they contend there is no need for uniformity. They would leave such interpretation and resultant rate determination to the courts.[6] Given

[5] Additional argument in regard to the state courts' award exceeding the area rate ceiling price is set out in III of this brief.

[6] This is inconsistent with the Commission's recent orders under the Natural Gas Policy Act of 1978, 92 Stat. 3350 (1978), confirming "the Commission's statutory responsibility to examine contracts covering gas subject to the Natural Gas Act." See, Order On Rehearing of Order No. 23, "Amendment and Clarification of the Commission's Interim Regulations Implementing the Natural Gas Policy Act of 1978 and Regulations Under The Natural Gas Act," 44 F.R. 30681 (May 29, 1979).

the primary aim of the *Natural Gas Act,* protection of consumers against exploitation at the hands of natural gas companies, and the Congressional intent of the Act to give the Commission jurisdiction over the rates of all wholesales of natural gas in interstate commerce, *Phillips Petroleum Co.* v. *Wisconsin,* 347 U.S. 672 (1954), Petitioner cannot imagine an issue that requires more uniformity than rate regulation under the *Natural Gas Act.* Indeed, Congress has charged the Commission to administer the *Natural Gas Act* in accordance with the policy of *Phillips.* And the Louisiana state courts, following parochial ideas of state law, have not only failed to consider but have openly and blatantly ignored the underlying purpose of the *Natural Gas Act*—the protection of the consumer.[1] The Commission must have had the opportunity to interpret Respondents' Rate Schedule with that aim as its primary objective. The Commission's role in this regard can and must intrude into state law if necessary to carry out the Commission's responsibilities under the *Natural Gas Act.* As this Court stated in *United Gas Improvement Co.* v. *Continental Oil Co.* ("*Rayne Field* case"), 381 U.S. 392, 400 (1965):

> "A regulatory statute such as the Natural Gas Act would be hamstrung if it were tied down to technical concepts of local law."

The Court noted that Louisiana law was in conflict with the Court's decision in that case because state law did not recognize a sale of gas in place. This decision illus-

[1] As Petitioner has shown in earlier briefs, the stated purpose of the Louisiana courts in their interpretation of Respondents' Rate Schedule was to protect the producer against a rise in the price of gas. See, Petition For Writ of Ceriorari filed in No. 78-986 on December 18, 1978, p. 21. Cf., *Atlantic Refining Co.* v. *Public Service Commission,* 360 U.S. 378, 393 (1959).

trates precisely the reason that the Commission should determine the meaning and legal effect of contracts for the sale of natural gas subject to the Commission's jurisdiction. The Commission determined in the *Rayne Field* case, largely on the basis of the dominant price reducing purpose of the *Natural Gas Act,* that the assignment, or sale, of developed oil and gas leases to an interstate pipeline was, under the *Natural Gas Act,* a sale of gas in interstate commerce. This Court affirmed the Commission's determination stating that a narrow interpretation of the *Natural Gas Act* would "make *Phillips* a shadow." 381 U.S. at 402.

A. The Paramount Nature of Federal Regulatory Law.

The Commission and the courts have recognized the paramount nature of the *Natural Gas Act* over jurisdictional transactions and that federal regulatory law controls as to such transactions. This federal law of Commission decisions and the decisions of the federal courts under the *Natural Gas Act* should be consistently applied to matters concerning producer rate increases for sales of gas in interstate commerce. Under the *Natural Gas Act,* when a gas purchase contract is filed with the Commission, it then takes on the character of a gas rate schedule and as such it is subject to the "paramount and exclusive authority" of the Commission. *Northern Natural Gas Co.* v. *State Corp. Commission,* 372 U.S. 84, 85, 92 (1963). The displacement of state law by federal regulatory law as to the interpretation of contracts on file as rate schedules regarding the triggering of a rate increase has been recognized in both court and Commission decisions. In *Superior Oil Co.* v. *El Paso Natural Gas Co.,* 377 S.W. 2d 691 (Tex. Ct. of Civ. App. 1964), the court was con-

fronted with a suit for a declaratory judgment seeking an interpretation of two purchase contracts containing favored nation clauses which Superior claimed had been triggered. The court held that the resolution of these matters was "preempted" by the application of federal regulatory law. In *Lone Star Gas Co.* v. *Howard Corp.*, 556 S.W.2d 372, 375 (Tex. Ct. of Civ. App. 1977), referring to *Superior Oil Co.*, the court stated:

> "The gas sales contracts of a natural gas company dealing in interstate commerce of gas for resale are controlled by the federal Natural Gas Act, 15 U.S.C.A.,Section 717, et seq. and are subject to the jurisdiction of and regulation of the Federal Power Commission. *Superior Oil* v. *El Paso Natural Gas Co.*, 377 S.W.2d 691; *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954)."

So, too, in *Appalachian Power Co.* v. *FPC, supra* at 347, it was held that the Commission had "properly treated [state] law as irrelevant to interpretation of the contract" on file as a rate schedule involving a triggering issue. In that case, the Commission had rejected the rate increase on the basis of *Mobile-Sierra, supra.* Responding to an argument that state law should control the interpretation of the rate schedule triggering issue, the Commission determined as follows, 49 F.P.C. 387, 388 (1973):

> "[S]tate law is not relevant to these wholesale rates, which are under the jurisdiction of the Federal Power Commission . . . Since the contracts are for the sale of electric energy at wholesale in interstate commerce, they are subject to the provisions of the Federal Power Act as interpreted by the Courts. APCO's proposal amounts to an allegation that such sales can be regulated by state law, which is not the case. *FPC* v. *Southern California Edison Co.*, 376 U.S. 205 (1964)."

Similar to these cases, this Court has recently rejected application of state law concepts to gas dedication issues under the *Natural Gas Act.* In *California* v. *Southland Royalty Co.*, 436 U.S. 519, 530-31 (1978), the Court stated:

> "We conclude that the Commission acted within its statutory powers in requiring that respondents obtain permission to abandon interstate service. 'A regulatory statute such as the Natural Gas Act would be hamstrung if it were tied down to technical concepts of local law.' *United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392, 400 (1965). By tying the concept of dedication to local property law, respondents would cripple the authority of the Commission at a time when the need for decisive action is greatest. Guided by *Sunray* [*Mid-Continent Oil Co.* v. *FPC*, 364 U.S. 137 (1960)], we believe that the structure and purposes of the Natural Gas Act require a broader view of the Commission's authority."

Also, the Tenth Circuit ruled in *Jicarilla Apache Tribe* v. *FERC*, 578 F.2d 289 (10th Cir. 1978), that "state law concepts of property interests created by oil and gas leases" are inapplicable to a regulatory determination by the Commission as to the jurisdictional rates to be charged by a small producer.[8] In relying on *Mobil Oil Corp.* v. *FPC*, 463 F.2d 256 (D.C. Cir. 1971), *cert. denied sub nom., Mobil Oil Corp.* v. *Matzen*, 406 U.S. 976 (1972), as the controlling federal

---

[8] The *Jicarilla Apache Tribe* decision demonstrates that the Commission's primary jurisdiction extends to the regulation of small producers, contrary to the Solicitor's assertion (Brief of the United States, p. 11). Cf., *FPC* v. *Texaco Inc.*, 417 U.S. 380 (1974).

rule of law,[9] the Tenth Circuit determined as follows as to the application of state law, 578 F.2d at 292:

> "[W]e need not, and do not, base our decision on state law concepts of property interests created by oil and gas leases . . . ."

More recently, the Fifth Circuit in *Tenneco Oil Co.* v. *FERC,* 580 F.2d 722 (5th Cir. 1978), referred to the Commission the issue of whether certain natural gas lease-sale agreements were sales of gas in interstate commerce within the meaning of the *Natural Gas Act.*

Other courts have recognized the need for uniformity in application by the Commission of federal regulatory law to producer rate increase filings, and particularly proposed rate increases under favored nation clauses. See *Ashland Oil and Refining Co.* v. *FPC,* 421 F.2d 17 (6th Cir. 1970); *Socony Mobil Oil Co.* v. *Brooklyn Union Gas Co.,* 299 F.2d 692, 695 (5th Cir. 1962), *cert. denied* 371 U.S. 887 (1962) ("[T]his Court does not have the authority to establish rates . . ."); *Mississippi Power and Light Co.* v. *Memphis Natural Gas Co.,* 162 F.2d 388, 390 (5th Cir. 1947), *cert. denied* 332 U.S. 769 (1947) ("To give effect to the 'Favored Nation' clause would operate to transfer the legislative function of ratemaking from the Commission to the courts."); *Bel Oil Corp.* v. *FPC,* 255 F.2d 548 (5th Cir. 1958); *Natural Gas Pipe Line Co.* v. *Harrington,* 246 F.2d 915, 918 (5th Cir. 1957) ("Nor does any court possess such power for the purpose of fixing retroactively a just, reasonable and lawful rate."); *Colorado Interstate Gas Co.* v. *FPC,* 324 U.S. 581 (1945); *Brooklyn Union Gas Co.* v. *Transcontinental Gas Pipeline Corp.,* 201 F.Supp. 673 (S.D. Tex. 1960); *McLeran* v. *El Paso Natural Gas Co.,* 357 F. Supp. 329, 331 (S.D. Tex. 1972), *affirmed,* 491 F.2d 405 (5th Cir. 1974) ("The federal courts lack the authority to determine a just and reasonable rate . . . [and] the courts may not fix a retroactive rate . . . .").

[9] See this brief *infra* at p. 19.

B. *Mobil Oil Corp. v. FPC* is Relevant to the Meaning of the Favored Nation Clause.

The Solicitor General and the Commission argue (Brief of the United States, pp. 14-15) that federal court decisions holding that leasing of gas producing properties is not a jurisdictional sale subject to the *Natural Gas Act* are not relevant to the meaning of the favored nation clause at issue in the case at bar. The Solicitor General and the Commission state that the fact that "such lease arrangements are not 'sales' " of gas within the Commission's jurisdiction under the *Natural Gas Act* does not preclude the conclusion that the parties intended them to constitute "purchase[s] within the meaning of their own contract and as a matter of state law." The Solicitor General and the Commission further argue that a state court decision in conflict with *Mobil, supra,* would not create an "imminent possibility of collision" between state court contract judgments and the Commission's authority to regulate interstate transportation and sale of the natural gas, citing as the sole reason for such statement that the Respondents have "claimed no damages in excess of rate ceilings established by Commission orders." [10]

The Solicitor General and the Commission have given a very narrow interpretation to *Mobil.* The language of the decision itself, 463 F.2d at 262, illustrates that

[10] See discussion of the claims of Respondents in this brief *infra,* p. 29.

the rule is not one limited to defining the scope of the Commission's jurisdiction but was set forth as a broad statement of federal regulatory law:

> "When we come to an ordinary lease by the landowner to the producer there is neither a "customary' sale in interstate commerce nor its equivalent in economic effect.
>
> . . . .
>
> To refer to the royalty owner as engaging in the sale is to depart from the common understanding of the words used, industry parlance, economic equivalent, or any other foundation . . . .
>
> [A]n economic interest in the proceeds of a sale, unaccompanied by authority to determine the incidents of the sale, does not make one a seller.

The term "sale" and its corollary "purchase," then, have the same meaning as to the scope of the Commission's jurisdiction and as to the common meaning of royalty transactions in substance and form. Indeed, it was the "common understanding of the words" that controlled the statutory construction in *Mobil.* It is for this same reason that the rule of *Mobil* is not one limited to defining the scope of the Commission's jurisdiction.

Further analysis of *Mobil* bears out the fact that the court clearly determined as a broad proposition of law that payment of a royalty by the lessee does not constitute a purchase of natural gas. In *Mobil,* the court relied heavily upon this Court's opinion in *Burnet* v. *Harmel,* 287 U.S. 103, 107 (1932):

> "[T]he statute speaks of a 'sale', and these leases would not generally be described as a 'sale' of the mineral content of the soil, using the term either in its technical sense or as it is commonly understood. Nor would the payments made by lessee to lessor generally be denominated the purchase price of the oil and gas. By virtue of the lease, the lessee acquires the privilege of exploiting the land for the production of oil and gas for a prescribed period; he may explore, drill and produce oil and gas, if found. Such operations with respect to a mine have been said to resemble a manufacturing business carried on by the use of the soil, to which the passing of title of the minerals is but an incident, rather than a sale of the land or of any interest in it or in its mineral content. *Stratton's Independence* v. *Howbert,* 231 U.S. 399, 414, 415; see *Von Baumbach* v. *Sargent Land Co.,* 242 U.S. 503, 521."

In applying the Supreme Court's opinion to the setting under the *Natural Gas Act* before it in *Mobil,* the court clearly determined, as a matter of federal regulatory law, that the payment of a royalty by the lessee does not constitute a purchase of natural gas.

Where there exists a body of regulatory law governing the meaning of certain terms which has evolved in a broader context than that of defining jurisdictional terms, it is inappropriate to limit the application of regulatory law on that basis. The Tenth Circuit's recent decision in *Jicarilla Apache Tribe* v. *FERC, supra,* is instructive in this regard. In a case concerning the appropriate rate to be charged by a small producer, the issue involved a determination of whether the lessor's election under a lease to take its royalty payments in kind rather than in cash was "tantamount to a purchase."

Both the Commission and the court looked to *Mobil* as the controlling federal regulatory rule of law and not as a decision limited to the scope of the Commis-

sion's jurisdiction. The court described the Commission's position as follows, 578 F.2d 292:

> "In its brief, the FERC argues that its ruling is supported by *Mobil* . . . That case held that lessors, royalty owners were not engaged in 'sales' of natural gas merely by accepting royalty payments pursuant to their leases. The FERC argues that this conclusion is correct because the entire ownership of the gas produced under the lease is in the lessee." [Footnote omitted.]

The court also referred to *Mobil* in reaching its conclusion, stating, *Id.*:

> "The conclusion in *Mobil Oil,* that royalty owners are not sellers of natural gas, was not based on any concept of ownership or title, however. See 463 F.2d at 259. The court found, rather, that a royalty owner was not a 'seller' in any commonly understood sense of that term. Our decision that the Tribe is not a purchaser of its royalty gas is based on much the same reasoning."

It is, therefore, particularly troubling that the Solicitor General and the Commission would argue that *Mobil* controls only as to the scope of the Commission's jurisdiction and that it does not apply to jurisdictional transactions themselves. That position is inconsistent with both Commission and court decisions which read *Mobil* as the controlling federal regulatory rule of law.

Petitioner submits that if the Louisiana court in 1961 or at any later time had referred the question of interpretation to the Commission, as it was bound under federal and state law to do, the plain terminology of the contract and the overwhelming unanimity of the courts in enforcing the primary purpose of the *Natural Gas Act* would have routinely called for an order from the Commission in favor of Petitioner.

By allowing the state courts of Louisiana to hold that a royalty payment was a "purchase of gas from another party seller" resulting in substantial price increases for the long period of time beginning in September, 1961, is to permit state courts and parochial views of state law to expand the term "sale" in favor of higher prices for the sale of interstate natural gas in past periods *without* the Commission determining these issues under the *Natural Gas Act.* The Louisiana courts' action is in violation of the *Natural Gas Act* and destroys uniformity of rate regulation by the Commission under that statute.

C. The Solicitor's Reliance on *Skelly* and *Pan American* is Misplaced.

The Solicitor General and the Commission rely heavily on two decisions of this Court, *Skelly Oil Co.* v. *Phillips Petroleum Co.,* 339 U.S. 667 (1950), and *Pan American Petroleum Corp.* v. *Superior Court,* 366 U.S. 656 (1961), to support the argument that the Commission's exercise of jurisdiction is not required in this case. An analysis of the two decisions reveals that neither of them is applicable to the issue of a producer rate increase under a favored nation clause of a Commission Rate Schedule.

(i) *Skelly Oil Co. v. Phillips Petroleum Co.*

The Solicitor General and the Commission argue that *Skelly* limits the applicability of the federal regulatory rule of law embodied in *Mobil* to issues of statutory construction (Brief of the United States, p. 12). In *Skelly,* a natural gas pipeline company had sought from the Commission a certificate of public convenience and necessity. In order to satisfy the prerequisite of adequate reserves of gas, the pipeline entered into a

contract to purchase gas from Phillips which in turn entered into contracts with Skelly, among others, to purchase gas for resale to the pipeline. The latter contracts contained a provision giving the sellers the right, after a certain date, to terminate the contract by notice given before issuance of a certificate by the Commission. Such notices were given two days after the Commission had ordered issuance of the certificate but before the actual content of the order was made public.

In construing the contract, the Court of Appeals equated the terms of the contract with that in the statute and assumed its problem to be the construction of what constitutes the "issuance" of a "certificate of public convenience and necessity" within the meaning of Section 7(c) of the *Natural Gas Act*, 15 U.S.C. § 717f(c). The Supreme Court remanded the case for a more thorough consideration of the application of the *Natural Gas Act*, and it suggested that the lower courts also consider the scope of the language in the construction of Section 7(c) of the *Natural Gas Act*, because the parties might not have intended to equate the statute and the contract. The Supreme Court stated in this context that the "parties do not necessarily endow statutory language in a contract with the scope of the statute, particularly when the same *term may have variant meanings for different applications of the statute.*" 339 U.S. at 678. (Emphasis added.)

At the outset it should be understood that *Skelly* did not involve any question as to the Commission's rate jurisdiction or the interpretation of a jurisdictional rate schedule. This is because at the time of the *Skelly* decision, 1950, the Commission did not yet exercise jurisdiction over producer sales. This Court's decision in *Phillips Petroleum Co.* v. *Wisconsin, supra,* did not

occur until several years later in 1954. Since the producer contracts were viewed as being non-jurisdictional they were not thought to be within the Commission's control and were not filed with the Commission. This fact which the Solicitor General and the Commission apparently have overlooked undercuts their argument that *Skelly* could limit the applicability of *Mobil* to issues of statutory construction. This is the case even apart from the showing by Petitioner that *Mobil* is a broad rule of federal regulatory law which is not so limited. Again, if the contracts in *Skelly* had been viewed as jurisdictional contracts they would have been on file with the Commission as rate schedules so that the interpretation of the term "issue" may have been treated differently. Cf. *Appalachian Power Co., supra.*

In any event, the interpretation of the term "sale" in *Mobil* does *not* have a "variant meaning" either "for different applications of the statute" (as was the case in *Skelly*) or even in common industry parlance.[11] *Mobil*, 463 F.2d at 262. In applying the Supreme Court's opinion to the setting under the *Natural Gas Act* before it in *Mobil*, the court clearly determined, as a matter of federal regulatory law, that the payment of a royalty by the lessee does not constitute a purchase of natural gas.

(ii) Pan American Petroleum Corp. v. Superior Court

The *Pan American* decision is inapplicable for reasons similar to the inapplicability of *Skelly*.

---

[11] So, too, the Commission had reached the same result in *Morris Mizel, et al., supra.* In that case, the Commission held that a farmout agreement did *not* constitute a "purchase" so as to activate a favored nation clause. See 30 F.P.C. at 1104.

Pan American did *not* concern the determination of the level of rates at which natural gas could have been sold for resale in interstate commerce. Rather, the Court in *Pan American* held that the state-court plaintiff was entitled to receive a *refund of payments which were over and above the rates on file* with the Commission under a Kansas minimum price law which was subsequently determined by the Supreme Court to be void *ab initio*. The suit was on a quasi-contract at common law by the pipeline purchaser, as plaintiff, to require a refund of these *excess* monies which the defendant-producers had exacted from the plaintiff under the minimum price law. The defendants urged that it was a claim arising under the *Natural Gas Act* of which the federal *courts* were given exclusive jurisdiction. It was actually a suit to recover monies that had been unlawfully collected from the pipeline. There was absolutely no question involved concerning the Commission's primary or exclusive jurisdiction regarding rates for the sale of gas in interstate commerce.

The basic question in *Pan American* was whether the pipeline's case should have been initiated in federal rather than state court. Since the plaintiff was seeking merely to be refunded excess payments above the established rate on file with the Commission, there was simply no statutory jurisdiction of the case in the federal courts. The case only involved the well-pleaded complaint rule of federal court jurisdiction. Cf. *Skelly Oil Co.* v. *Phillips Petroleum Co., supra,* and *Gully* v. *First National Bank,* 299 U.S. 109, 112, 113 (1936). The plaintiff had pleaded a state cause of action—refund of monies allegedly overpaid to defendant. 366 U.S. at 662-63.

If the issue in the present proceeding were whether Respondents (as plaintiffs in the state court) could

have instituted their case in federal court, then *Pan American* might have some application.[12] However, it has utterly no application to the primary and exclusive rate jurisdiction of the Commission.

In *Lewis* v. *Transcontinental Gas Pipe Line Corp.,* 200 F.Supp. 219, 220 (S.D. Tex. 1961), *Pan American* was urged as a defense in a suit to determine the scope of a certificate of public convenience and necessity issued by the Commission. The issue in the case was whether the plaintiff must exhaust his administrative remedies with the Commission prior to seeking judicial relief. The court recognized that *Pan American* did not apply to the determination of agency versus court jurisdiction:

> "We do not think said case is controlling here. In that case, the Supreme Court did not deal with the question of administrative remedies or the exhaustion of the same. That case involved purely and simply a question of Federal v. State jurisdiction; or more simply stated, the question of whether a Federal Court or a State Court had jurisdiction of the case."

Clearly, *Pan American* has no application here. Respondents in the instant case sought in the Louisiana

---

[12] Again, however, *Pan American* involved a suit to refund overcharges or collections in excess of the rate on file with the Commission, which is different from Respondents' state court action here in *seeking an increase in rate levels. Pan American* would have direct application to the instant case only if Respondents were suing for a refund of excess collections. There is a major jurisdictional difference between a suit to recover overcharges or collections in excess of the rate on file with the Commission and Respondents' state court action in seeking an increase in rate levels. The difference is explained in *Socony Mobil Oil Co.* v. *Brooklyn Union Gas Co., supra,* and in Petitioner's Reply Brief of January 29, 1979 at page 6, n. 7.

state courts an increase in the rate at which natural gas has been sold by them to Petitioner, under the authority of a Certificate and Rate Schedule controlled by the Commission for the long period 1961 through 1975. No court, either federal or state, has the power to determine the price at which the sale of interstate natural gas can be made, that function being exclusively delegated to the Commission under specific directive from the United States Congress in the *Natural Gas Act*. See, *supra*, pp. 18-19. Respondents' claim for an increase in the price at which gas was sold during this period of time should have been properly submitted to the Commission in the first instance because the Commission is the administrative body with the primary and exclusive adjudicative responsibility for the determination of the rates at which natural gas is to be sold in interstate commerce.

III.

THE STATE COURT DECISIONS INFRINGE ON THE COMMISSION'S REGULATORY RESPONSIBILITIES UNDER THE NATURAL GAS ACT

Not only have the decisions of the Louisiana courts infringed upon the jurisdiction of the Commission and its regulatory responsibilities under the *Natural Gas Act* by having given effect to a favored nation clause of Respondents' Rate Schedule without a determination by the Commission that such activation of the favored nation clause is consistent with the federal regulatory law or that such activation would be within the public interest under the *Natural Gas Act;* but also, (1) the Louisiana courts have determined, in violation of the *Natural Gas Act,* the rate at which natural gas could and should have been sold in interstate commerce for the entire period September, 1961, through December,

1975; (2) the Louisiana courts have assumed that Respondents' calculations and adjustments for the purposes of comparing Respondents' Rate Schedule with the Government lease transaction are in accordance with the *Natural Gas Act;* and (3) the Louisiana courts have assumed that Respondents' claims for the period 1961 through 1975 would not exceed the applicable area or ceiling rates promulgated by the Commission under the *Natural Gas Act*. These actions by the Louisiana courts are in direct conflict with the *Natural Gas Act* and the regulations of the Commission.

Of particular significance in the case is the treatment of liquefiable hydrocarbons (or "extractible liquids," an interchangeable term). See pp. 10-12, *supra*. The Respondents have cast their claim as a separate claim for "residue gas" and "extracted plant products" for the very purpose of avoiding the *Natural Gas Act*. An inspection of Respondents' Rate Schedule (see pp. 10-11, *supra*) shows that Respondents sell raw wet gas at the wellhead for a price slightly higher than they would have received had the contract contained means whereby they could be paid for extracted products. See, *Sunray Mid-Continent Oil Co.* v. *FPC,* 290 F.2d 552 (10th Cir. 1961). The sale is a sale of raw wet gas with all of the liquefiable hydrocarbons contained therein. Respondents have claimed that payments for liquefiable hydrocarbons contained in the gas as sold to Petitioner are payments for "extracted products" and thus are not subject to Commission jurisdiction under the *Natural Gas Act*. However, *Natural Gas Act* jurisdiction clearly covers this wellhead sale of natural gas and all the entrained liquids. *Permian Basin Area Rate Case,* 390 U.S. 747, 820 (1968); *Mobil Oil Corp.* v. *FPC,* 483 F.2d 1238, 1249 (D.C. Cir. 1973); *El Paso*

Natural Gas Co., 29 F.P.C. 1175, 1179-80 (1963). The Examiner's decision in the latter case stated as follows, 29 F.P.C. at 1207-08:

> "What is sold and delivered under these contracts is not liquid hydrocarbons at all, but is natural gas, all of which is delivered at the mouth of the wells or at the outlet of the separator (if one is installed at the wellhead)."

Thus, Respondents and the Louisiana courts have made a change in their Rate Schedule without Commission approval providing for a separate settlement of "extracted products" and "residue gas" when in fact the sale under the Rate Schedule was of wet gas and all liquefiable hydrocarbons contained therein. ***There is no sale of "extracted plant products" or "residue gas."***

Under the *Natural Gas Act*, the only way in which this Rate Schedule could have been changed is by agreeing with the Petitioner as to a change in the contract and filing such agreement with the Commission as a supplement to the Rate Schedule. *Sunray Mid-Continent*, 290 F.2d at 555. Respondents have not done so, but rather, have sued in state court for an alteration of the terms of the contract to provide for the circumstances of a sale of extracted plant products and residue gas, when, in fact, the sale was of raw wet gas at the wellhead.

The purpose for which Respondents have made such a claim is that the royalties paid to the Government on gas produced by Petitioner were based on separate values of residue gas and extracted plant products after processing. It is by converting the sale by Respondents to Petitioner under the Rate Schedule from a wellhead sale to a transaction exactly like the royalty transaction that the Respondents have, in effect, avoided compliance with the *Natural Gas Act*.

The Solicitor General and the Commission's position in deferring to the erroneous interpretation by the Louisiana state courts as to what constitutes a wellhead sale places unlawful limits on the Commission's rate jurisdiction over extractible liquids in violation of *Phillips Petroleum Co.* v. *Wisconsin, supra.* Cf., *Tenneco Oil Co.* v. *FERC, supra.* To interpret a contract for the sale in interstate commerce of gas containing extractible liquids as permitting an additional price for the extractible liquids above the applicable wellhead area rate ceiling would totally defeat the purpose of the *Natural Gas Act*. That is what the Louisiana state courts' interpretation of the contract in this case will do.

IV.

CONCLUSION

Congress conferred upon the Commission exclusive jurisdiction under the *Natural Gas Act* to determine the rates at which natural gas could be sold in interstate commerce for resale. The Louisiana state courts have infringed upon that jurisdiction. First, they failed to refer the case to the Commission for decision. Then, they made determinations of the applicable rate for past periods. If state courts may interpret gas rate schedules in conflict with the *Natural Gas Act* and, if the state courts may determine the rate at which natural gas could have been sold during past periods, the very purpose for which the *Natural Gas Act* was enacted, protection of the consumer, will be jeopardized by the efforts of state courts to protect local policies and interests.

Respectfully submitted,

ROBERT ROBERTS, JR.
MARLIN RISINGER, JR.
W. MICHAEL ADAMS

BLANCHARD, WALKER, O'QUIN & ROBERTS
Post Office Drawer 1126,
Shreveport, Louisiana 71163

Counsel for Petitioner

REUBEN GOLDBERG
GLENN W. LETHAM
GOLDBERG, FIELDMAN & LETHAM, P.C.
1700 Pennsylvania Ave., N.W.
Washington, D.C. 20006

Of Counsel